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C O N F I D E N T I A L SECTION 01 OF 02 MINSK 000250

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SUBJECT: GOB LIKELY TO SEEK LOANS BEFORE FDI

REF: A. MINSK 216  
[B.](#) MINSK 188  
[C.](#) 06 MINSK 1220

Classified By: Charge Jonathan Moore for reason 1.4 (d).

Summary

[11.](#) (C) While higher energy prices have not immediately impacted all firms significantly, Belarusian manufacturers have become less competitive. As a result, the GOB will seek to reduce imports. Bureaucratic and philosophical barriers will prevent drawing foreign investment into Belarus via serious privatization. Consumer spending also looks unlikely to boost the economy. Foreign lending will likely postpone serious reform, for which Lukashenko's inner circle does not recognize the need, until at least 2009 and possibly after Lukashenko's seeks re-election in 2011. End summary.

[12.](#) (C) This cable draws upon a number of sources, including comments from local businesspeople at a March 16 lunch with the Ambassador in the northern city of Polotsk. Invited Polotsk entrepreneurs included Vladimir Zakharov, whose businesses include retail outlets, construction, cable television and a newspaper; Pyotr Livshits, the owner of a wholesale food processor; Aleksandr Volkov, whose owns a fish processing plant; and Ruslan Tabachnikov, who has a small chain of car repair and carwashes. Also, Pol/Econ Chief on March 16 hosted a breakfast with Aleksandr Yaroshevich, Director General of Coca-Cola Bottlers Belarus; Aleksandr Chubrik of the Institute for Privatization and Management; Yelena Chizhik from the Belarusian Union of Entrepreneurs; economics professor Mikhail Zalesskiy, formerly of the Ministry of Economics' Research Institute; Roman Osipov, Head of Investment at Uniter Consulting; Leonid Zlotnikov of the Institute for Social Issues; and Sergey Balykin of the independent business weekly "Bela rusy i rynok".

Private SMEs Not Feeling Higher Energy Prices Yet

[13.](#) (C) The Ambassador's visit with entrepreneurs in Polotsk demonstrates that if given a chance, the private sector -- which currently accounts for just 20 percent of employment in Belarus -- could succeed. Unlike massive state-owned enterprises, their businesses do not rely primarily on huge energy subsidies. Tabachnikov was optimistic the higher price of gasoline would not impact his car repair business significantly. Zakharov reported only a two-percent rise in the cost of product at his distillery. Livshits noted his warehouses use energy very efficiently. Volkov suggested there would be a market in Belarus for more U.S. imports.

## But Most Belarusian Products Becoming Less Competitive

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**¶14. (C)** During the breakfast with Pol/Econ Chief, Zlotnikov predicted zero GDP or even a decrease this year. He described Belarusian manufacturers as becoming less and less competitive against those in Russia. Even in machine building, one of Belarus' traditional strengths, Russian producers were beginning to overtake Belarusian ones due to higher levels of investment. Chizhik said even in some areas where there was demand in Russia for Belarusian products, such as processed food, over regulation and complicated customs procedures prevented small businesses from exporting. Most worryingly for the economy, Zlotnikov said Belarus lacked attractive investment opportunities for foreign or even domestic companies.

## Leading to a Crackdown on Imports

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**¶15. (C)** Balykin explained how the inefficiency of Belarusian manufacturers resulted in regulations to restrict entrepreneurs (ref A). Large state-owned companies understand they cannot sell their products even domestically and lobby the government to suffocate small traders earning a living from selling imports. Balykin agreed with Zlotnikov that investment opportunities were few and far between, mentioning bloated social infrastructure costs associated with large enterprises and the inability to lay off redundant staff.

## Medium-sized Acquisitions Still Require Big Shot Approval

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**¶16. (C)** Despite noises the government may begin a round of privatizations (ref B), Osipov noted the bureaucratic barriers to investment. Even acquiring a minority stake in a medium-sized state-owned enterprise requires the go ahead from Lukashenko or people close to the dictator. What is more, if approval is given, that does not mean the investor can be assured the Belarusian government will take the responsibility to ensure a level-playing field for the enterprise in the future. Osipov sounded even more certain than he did in January that Gazprom's investment in a joint venture with Beltransgaz would fall through for precisely this reason (ref B).

## Less Money Circulating

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**¶17. (C)** Yaroshevich said that despite large investments predicated on expected sales growth of 15 percent, Coca-Cola sales in Belarus were down one percent for the year through February. Sales in February were worse than in January. Yaroshevich believes the first utility bills of 2007, which increased 30 percent, scared consumers. Osipov suggested the significant rise in real estate prices so far this year indicated well-off Belarusians were looking for a safe investment. He added that banks were tightening up on credit to small businesses.

## GOB's Room for Maneuverability: Loans and Wage Stagnation

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**¶18. (C)** Chubrik cautioned against accepting on face value rumors the economy was headed for an imminent collapse. He said the government could seek foreign loans over the next two to three years without much difficulty given that current foreign debt totaled less than two percent of GDP. Also, with presidential elections four years away, the government will keep wage increases low.

## Socialist Mentality Prevents Real Reform

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¶9. (C) Zalesskiy explained that too many of those in positions of power learned what little economics they know from Karl Marx. They simply want factories to run. The recent trips to Venezuela, Cuba and elsewhere were Lukashenko's attempts to look for a handout. Osipov cited Deputy Prime Minister Vladimir Semashko, the former General Director of the television manufacturer Gorizont, as an example. He was promoted after supposedly turning around the enterprise, but actually he was just successful in obtaining budget subsidies and Gorizont remains a mess. Zalesskiy echoed Chubrik's statement that the government would not consider significant privatizations until two or three years down the road, when the regime depletes its foreign reserves.

Comment: Import Substitution Destined to Fail

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¶10. (C) Taking on increased foreign debt to invest in competitive sectors of the economy would represent a sound policy. Unfortunately for Belarusians, under current conditions any investment would bring negligible returns. Previously the GOB "invested" high profits from arbitrage on oil and gas into maintaining the flow of cheap energy from Russia (ref D). Lukashenko will probably use whatever revenues come his way to buy friends and lobby Moscow for cheaper energy and privileged access to the Russian market.  
Moore